

Responsibility of the accounting officer for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the basis of accounting and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (M/FMA). This responsibility includes:

- designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
- selecting and applying appropriate accounting policies
- making accounting estimates that are reasonable in the circumstances.

Responsibility of the Auditor-General

3. As required by Section 188 of the Constitution of the Republic of South Africa, 1996 read with Section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and Section 126(3) of the M/FMA, my responsibility is to express an opinion on these financial statements based on my audit.

4. I conducted my audit in accordance with the International Standards on Auditing. Those standards require that I comply with the ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

5. An audit involves performing procedures to obtain evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

6. An audit also includes evaluating the:
- appropriateness of accounting policies used
 - reasonableness of accounting estimates made by management
 - overall presentation of the financial statements.

7. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis of accounting

8. The Municipality's policy is to prepare financial statements on the entity-specific basis of accounting as set out in accounting policy note 1.

Basis for qualified opinion

Irregular Expenditure - Travel Allowances Overpaid

9. Gross travel allowances totalling R 844,634 were overpaid to councillors during the financial year under review since the councillors further received motor car allowance. These payments are considered irregular due to the incorrectly implementation of government gazette no. 28990, notice No. R653 and No. 1224 based on section 7(1) of the Remuneration of Public Office Bearers Act, 1998 (Act No. 20 of 1998), which only allowed a motor vehicle allowance to be paid to councillors. This has resulted in an understatement of debtors of R 844,634 and the net deficit for the year being overstated by the same amount.

Limitation of scope - Supporting Documentation for Expenditure

10. Supporting documentation in respect of general expenditure totalling R 817,174 was not made available by the municipality for audit purposes. I am therefore unable to verify the validity, accuracy and completeness of these expenditure payments.

Unauthorised expenditure

11. The total actual expenditure of R 53.5 million exceeded the total budgeted expenditure of R 48.9 million resulting in unauthorised expenditure of R 4.6 million. The notes to the annual financial statements did not disclose unauthorised expenditure as required by section 125(2)(d)(i) of the MFMA.

Qualified opinion

12. In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraphs, the balance sheet of Umhlabyalingana Municipality as at 30 June 2007 and its income statement and cash flow statement for the year then ended have been prepared, in all material respects, in accordance with the basis of accounting as set out in the accounting policies note 1 to the financial statements and in the manner required by the MFMA.

Emphasis of matters

I draw attention to the following matters:

Going concern

13. Note 12 to the financial statements indicates that Umhlabyalingana Municipality incurred an operating deficit of R 8,5 million for the year ended 30 June 2007 and as at that date the entity's total liabilities exceeded its total assets by R 1,2 million. These conditions, along with other matters, point to the existence of a material uncertainty that may cast significant doubt on the entity's ability to continue as a going concern.

Significant Uncertainty

14. Value Added Tax Refund

A Value Added Tax (VAT) refund from the South African Revenue Service (SARS) totalling R 3,8 million will only be repaid to the municipality upon the completion of a VAT audit by the SARS. I was unable to establish the facts and circumstances surrounding the delay in the VAT refunds from SARS and unable to assess the likelihood of whether the amounts will be refunded by SARS. Consequently, assets may be overstated by R 3,8 million should this amount not be refunded by SARS.

OTHER MATTERS

I draw attention to the following matters that are ancillary to my responsibilities in the audit of the financial statements:

Non-compliance with applicable legislation

Municipal Finance Management Act

15. The municipality has not complied with section 32 (1) (d) and 32 (4) (a) to (c) of the MFMA, in not having implemented procedures for the recovery of an amount of R 418,464 owing by the previous accounting officer. Furthermore, an amount of R 289,383 relating to cellphone allowances that were overpaid to certain councillors in respect of the financial year ended 30 June 2005 had not been recovered by the municipality neither had any steps been taken for the recoverability of these funds.
16. The municipality has not developed and implemented a risk management and internal control framework relating to fraud prevention in accordance with section 62(1)(c)(i) of the MFMA.
17. The municipality has not complied with section 71 of the MFMA that requires the accounting officer of the municipality to submit within 10 working days after each

month end, a monthly budget statement in the prescribed format to the Mayor and the relevant Provincial Treasury.

18. The municipality has not complied with section 72 of the MFMA requiring a mid-year budget and performance assessment. The significant operating deficit experienced in the 2006/2007 financial year may have been averted had this assessment been timely undertaken and expenditure scaled down in proportion to the remaining budget.

19. The municipality has not complied with section 79 of the MFMA in that no delegation of authority has been developed.

Matters of governance

20. During the review of the councillors' declarations of interest form it was noted that 14 out of a total of 26 councillors had not declared their interest.

21. Related party transactions to the value of R271,227 was not disclosed in the annual financial statements. These transactions relate to a contract awarded to a Close Corporation in which the Mayor has a significant member's interest. No written declaration of interest was made by the mayor. Furthermore, a related party register is not maintained by the municipality.

Material corrections made to the annual financial statements initially submitted for audit

22. The annual financial statements approved by the Municipal Manager and submitted for audit on 31 August 2007, have been significantly revised in respect of the following material misstatement identified during the audit:
- 22.1 A total of R12,1 million was initially transferred directly from various reserve accounts to fixed assets as these accounts were not intended for capital expenditure.

Upon revision and correction of the annual financial statements, the amount transferred from reserves to operating income totalled R8,9 million and contribution to reserves during the year of R4,2 million being brought into account. The net effect was an increase in reserves by R7,4 million and operating deficit increasing by the same amount.

- 22.2 The Cash Flow Statement was materially incorrect. The prior year comparatives did not agree to the audit annual financial statements and Investments in fixed assets was reflected as nil when fixed assets in that set of annual financial statements had increased by R14,7 million.

- 22.3 Contribution to the capital development fund was initially stated at R 2 million. This was reduced to R 599,839 resulting in the decrease of R1,4 million in the capital development fund and the operating deficit.

22.4

Councillors' allowances as disclosed in the annual financial statements under Note 13 initially reflected an amount of R1,1 million and was understated by R2,1 million. The note has been adjusted to reflect the correct amount of R3,2 million.

22.5

Appendix D of the annual financial statements did not initially include any

comparative figures for operating income in respect of the prior year. This was subsequently adjusted to reflect the correct comparatives.

22.6

An amount of R 650,222 was initially written-off to bad debts without adequate justification and council approval.

The subsequent correction to the annual financial statements resulted in debtors increasing by R 650,222 and bad debts/operating deficit decreasing by the same amount.

Due to the uncertainty with regard to the recoverability of this debt, a provision for doubtful debts was thereafter raised for the full amount resulting in an increase of R 650,222 in operating deficit and the provision for bad debts.

Internal Control

23.

Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes of the matters indicated, as they relate to the five components of internal control. In some instances deficiencies exist in more than one internal control component.

Reporting Item	Control Environment	Assessment of Risks	Control Activities	Information and Communication	Monitoring
Basis for qualification					
Irregular expenditure - travel allowance overpaid			✓		
Limitation of scope – supporting documentation for expenditure			✓		
Unauthorised expenditure			✓		
Emphasis of matter					
Going concern					
VAT refund			✓		✓
Other matters					
Non-compliance with applicable legislation	✓		✓		
Matters of governance			✓		
Material corrections to the annual financial statements			✓		

Unaudited supplementary schedules

24. The supplementary information set out on pages 13 to 18 does not form part of the annual financial statements and is presented as additional information. I have not audited these schedules and, accordingly I do not express an opinion on them.

OTHER REPORTING RESPONSIBILITIES

Reporting on performance information

25. I was engaged to audit the performance information.

Responsibility of the accounting officer for the performance information

26. In terms of Section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of Section 45 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

Responsibility of the Auditor-General

27. I conducted my engagement in accordance with Section 13 of the PAA, 2004 (Act No. 25 of 2004) read with General Notice 646 of 2007, issued in Government Gazette No. 29919 of 25 May 2007 and section 45 of the MSA.
28. I was not provided with the necessary information, documentation and explanations timeously with regard to the performance information system. Consequently, I was unable to conduct our audit of performance information.

Late finalisation of the audit report

29. In terms of Section 126(3)(b) of the MFMA, the Auditor-General is required to submit the audit report to the accounting officer within three months of the receipt of the annual financial statements. In the interest of improving accountability and due to the process implemented to ensure consistency in the manner in which material audit findings are reported, I have delayed the finalisation of the audit report to the date reflected on the audit report.

APPRECIATION

30. The assistance rendered by the staff of Umhlabuyalingana Municipality during the audit is sincerely appreciated.

Nathan General
Pietermaritzburg

25 April 2008



AUDITOR-GENERAL